No. 3961

IN THE

# UNITED STATES
# CIRCUIT COURT OF APPEALS
## FOR THE NINTH CIRCUIT

In the Matter of PATTERSON-MacDONALD SHIPBUILDING COMPANY, a Corporation, Bankrupt,

COMMONWEALTH OF AUSTRALIA,
*Petitioner,*

*vs.*

A. M. MacDONALD and JOHN L. McLEAN, as Trustee in Bankruptcy of Patterson-MacDonald Shipbuilding Company, a Corporation, Bankrupt.
*Respondents.*

# BRIEF OF PETITIONER
## In Petition

**Under Section 24b of the Bankruptcy Act of Congress Approved July 1, 1898, to Revise, in Matter of Law, a Certain Order of the United States District Court for the Western District of Washington, Northern Division**

CORWIN S. SHANK
*Attorney for Petitioner*

1002 Alaska Building Seattle, Washington

Press of Pliny L. Allen Co., Seattle

IN THE

# UNITED STATES
# CIRCUIT COURT OF APPEALS
## FOR THE NINTH CIRCUIT

---

In the Matter of PATTERSON-MacDONALD SHIPBUILDING COMPANY, a Corporation, Bankrupt,

COMMONWEALTH OF AUSTRALIA,
*Petitioner,*

*vs.*

A. M. MacDONALD and JOHN L. McLEAN, as Trustee in Bankruptcy of Patterson-MacDonald Shipbuilding Company, a Corporation, Bankrupt.
*Respondents.*

---

# BRIEF OF PETITIONER
## In Petition

**Under Section 24b of the Bankruptcy Act of Congress Approved July 1, 1898, to Revise, in Matter of Law, a Certain Order of the United States District Court for the Western District of Washington, Northern Division**

---

On March 19, 1920, the Patterson-MacDonald Shipbuilding Company was duly adjudged a bankrupt in the United States District Court for the Western District of Washington, Northern Division, upon its voluntary petition. The matter was referred to the

Honorable Cicero R. Hawkins as Referee in Bankruptcy and the respondent, John L. McLean, was duly elected trustee of the said bankrupt. Prior to the bankruptcy, the respondent, A. M. MacDonald had been a stockholder, official and chief managing agent of the bankrupt, (Record p. 9) and also the man who was familiar with the details of the business of the bankrupt.

At the time of the bankruptcy, the bankrupt had a large claim against the United States Shipping Board, Emergency Fleet Corporation, and the Commonwealth of Australia had a large claim against the bankrupt. The trustee and his attorneys made considerable use of Mr. MacDonald in prosecuting the claim of the trustee against the Emergency Fleet Corporation and in defending against the claim of the Australian Government. The result of the combined efforts of the trustee and his attorneys with the assistance of the information furnished by Mr. MacDonald, extending over more than a year's time, was that the claim of the trustee against the Emergency Fleet Corporation was settled by a cash payment of $277,253.74, together with various other terms favorable to the trustee equivalent to about $50,000, (Record p. 16), and the claim of the Commonwealth of Australia was rejected by the District Court and is now pending on appeal in this court. Respondent A. M. MacDonald during the progress of the proceedings had received from the trustee, pursuant to orders of the court, $6500 on account of "expenses and services".

On July 20, 1922, respondent A. M. MacDonald presented to the trustee a bill in the form of a letter for $20,000 (additional to the $6500) as compensation for his services rendered in the prosecution of the claim against the Shipping Board and the defense of the claim against the Commonwealth of Australia. To this claim the petitioner interposed its objections, but such objections were overruled and the referee made to Mr. MacDonald an allowance of $20,000 in a lump sum for his services and expenses, without any segregation of what was for his expenses from what was for his services, or of what services were in connection with the claim of the Shipping Board from what were his services in connection with the claim of Australian Government .

This petitioner thereupon filed its petition for review in the District Court (Record pp. 20-23) in which petition for review this petitioner claimed that the said rule and order of the referee were erroneous for the following reasons:

1. There was no sworn statement, either oral or written, and no itemized statement of any kind made to form the basis of any claim herein as required by the bankruptcy act and the rules, and the practice of this court.

2. That there is no segregation in the order of the items, so it is impossible to determine how much was allowed the said A. M. MacDonald for expenses actually incurred and how much for services rendered, or

how much was allowed the said A. M. MacDonald for each service rendered.

3. That the said trustee or his attorneys were never authorized either by the referee or the creditors of the said bankrupt to agree, either expressly or impliedly, to pay the said A. M. MacDonald any sum whatsoever for services to be rendered by the said A. M. MacDonald.

4. That the said A. M. MacDonald rendered no services whatsoever other than what he was expressly required to render under the bankruptcy act.

5. That it is contrary to the letter and spirit of the bankruptcy act and the rules and the practice of this court to pay an officer of the bankrupt for imparting information regarding the business matters and affairs of the bankrupt.

6. That the said allowance is excessive.

During the hearing before the District Court, on account of the somewhat indefiniteness of the referee's certificate, it was stipulated by the parties (Record p. 9) that the said respondent, MacDonald, was at and prior to the adjudication of the bankruptcy of the said bankrupt, a stockholder, officer and chief managing agent of the bankrupt, that no sworn statement had ever been made regarding the nature of the services rendered by the said A. M. MacDonald in the said bankruptcy proceeding, that there had been no segregation in the allowances for payment of expenses and for services, or for services in the matter of the two cases

and that in the event of the claim of the Commonwealth of Australia being finally rejected there would be a substantial sum of money left after paying all claims of creditors to be returned to the bankrupt corporation. Also at the hearing the said A. M. MacDonald was directed to file a sworn statement itemizing his expenses and this sworn statement, filed in accordance therewith, segregated his expenses by ascribing exactly $214.50 to each one of four trips between Seattle and Washington, exactly $7.50 for each day for his hotel bills, exactly $5.50 for each day's meals, exactly $2.00 for each day's tips and exactly $4.50 for "other miscellaneous expenses, including luncheons, dinners, laundry, automobiles, etc.", making a total of expenses of exactly $19.00 for each day consumed upon his trip to Washington (Record p. 11).

Upon the hearing had, however, the District Court entered its order, approving, sustaining and confirming the order of the referee in every respect. To this order this petitioner took due and proper exception and subsequently filed its petition in this court.

## Specifications of Error Relied Upon

We respectfully submit that the order of the District Court was erroneous in the following particulars:

First: The court erred in not sustaining the objections of these claimants to the said order of the said referee on the ground that there was no segregation in

the order of the items so that it was impossible to determine from the said order how much was allowed the said A. M. MacDonald for expenses actually incurred and how much for services rendered, or how much was allowed the said A. M. MacDonald for each service rendered.

Second: The court erred in not sustaining the objections of these claimants to the said order of the said referee on the ground that the said John L. McLean, trustee, in bankruptcy, nor his attorneys, were never authorized either by the referee or the creditors of the said bankrupt to agree, either expressly or impliedly, to pay the said A. M. MacDonald any sum whatever for services to be rendered by the said A. M. MacDonald.

Third: The court erred in not sustaining the objections of these claimants to said order of the said referee on the ground that the said A. M. MacDonald rendered no services whatsoever other than what he was expressly required to render under the bankruptcy act.

Fourth: The court erred in not sustaining the objections of these claimants to said order of the said referee on the ground that it is contrary to the letter and spirit of the bankruptcy act and the rules and practice of this court to pay an officer of the bankrupt for imparting information regarding the business matters and affairs of the bankrupt.

Fifth: The court erred in not sustaining the objections of these claimants to said order of the said

referee on the ground that the said allowance is excessive.

Sixth: The court erred in approving the order of the referee ordering payment to the said A. M. MacDonald in the sum of $13,500.00.

## ARGUMENT

All the above specifications of error merely go to the one proposition, and that is, that the order of allowance in question was erroneous. The claim for expenses is palpably and evidently false upon its face. It might be that Mr. MacDonald spent the entire sum of money upon this trip which he claims that he spent, but it would be absolutely impossible that he spent exactly $2.00 on each and every day of his trip for tips, or exactly $5.50 on each and every day for meals, or exactly $4.50 on each and every day for incidentals.

When it comes to the question of services, the record is equally obscure.

The services rendered were absolutely intangible. Just what he did or how he did it was absolutely left unexpressed. The referee, however, states in his certificate that these services were "absolutely essential to the successful preparation and prosecution of said claim." It is not claimed that these services were rendered as an attorney or even as a technical engineering expert. In the face of the finding of the referee it

cannot be so claimed for the reason that however pre-eminent any individual might be, either as an attorney or as an engineering expert, it is absolutely impossible that no other person could not be found to take his place. The only possible explanation of the statement that Mr. MacDonald's services were "absolutely essential" that can be made is that Mr. MacDonald in his capacity as chief managing agent of the bankrupt had acquired and still retained details of the business which it was absolutely essential for the trustee and his attorneys to get in order to prosecute the one claim and defend against the other. In other words, the chief managing agent of the bankrupt had certain facts and it was necessary to bribe such managing agent and bribe him very liberally in order to get him to divulge those facts .

The Bankruptcy Act, however, meets this situation. Section 1 (19) of the Bankruptcy Act provides that: " 'persons' shall include corporations, except where otherwise specified, and *officers,* partnerships, and women," while § 1 (4) provides that " 'bankrupt' shall include a *person* against whom an involuntary petition or an application to set a composition aside or to revoke a discharge has been filed, or who has filed a voluntary petition, or who has been adjudged a bankrupt"; while § 7 (a) of the Bankruptcy Act provides that "the bankrupt shall * * * (3) examine the correctness of all proofs of claims filed against his estate * * * (7) in case of any person having to his knowledge proved a false claim against his estate,

disclose that fact immediately to his trustee * * * and (9) when present at the first meeting of his creditors, and at such other times as the court shall order, submit to an examination concerning the conducting of his business, the cause of his bankruptcy, his dealings with his creditors and other persons, the amount, kind and whereabouts of his property, and, in addition, all matters which may affect the administration and settlement of his estate; * * * Provided, however, that he shall not be required to attend a meeting of his creditors, or at or for an examination at a place more than one hundred and fifty miles distant from his home or principal place of business, or to examine claims except when presented to him, unless ordered by the court, or a judge thereof, for cause shown, and the bankrupt shall be paid his actual expenses from the estate when examined or required to attend at any place other than the city, town or village of his residence."

We thus see that both within the letter and the spirit of the Bankruptcy Act it is the duty of an official of a corporate bankrupt as much as of an individual bankrupt to furnish to the trustee all the information which he may have relative to the business affairs of the bankrupt so as to enable the trustee to administer the affairs of the bankrupt to the best possible advantage.

When the Patterson-MacDonald Shipbuilding Company became bankrupt its business was very much involved, but such a situation is very frequent in the bankruptcy courts In order to administer an estate

it is absolutely essential that the trustee should have the benefit of all the information that the officers and employees of the bankrupt may be able to give him, and the Bankruptcy Act provides that the trustee may compel such information. It is true that the officers of the bankrupt can not be compelled to attend at other than certain places or at certain distances, but that is a provision that may be waived by the officer and upon attending at a distance, there is no question but what he is entitled to his expenses when properly claimed and he might also be entitled to a witness fee. Upon this theory the present petitioner made no objection to the various court orders which allowed Mr. MacDonald an aggregate of $6500 on account of his expenses and services upon his extensive trips to Washington. It will be noticed, however, that none of these orders were a formal adjudication as to the amount he was to receive or a waiver of the right to insist upon a strict accounting as to his expenses. They were made merely on account, with the expectation that a proper expense account would subsequently be filed.

But is this court going to lay it down as a rule of law that the bankrupt of an estate which is involved in litigation can withhold the information which he has regarding the subject matter of that litigation until he receives from the trustee what he considers ample compensation for the furnishing of such information? If such is the law, it will be the first time it has ever appeared in the decision of any bankruptcy case, and it will open the door to a throng of claims on the part of

individual bankrupts and officers of corporate bankrupts for compensation for assisting the trustee in litigation regarding their estates.

But whatever might be said in favor of making to Mr. MacDonald an allowance as compensation for his trip to Washington, the same does not apply to giving him compensation for his services in connection with contesting the claim of the Australian Government. Under the Bankruptcy Act it is the express duty of a bankrupt to "examine the correctness of all proofs of claims filed against his estate" § 7 (3) "immediately inform his trustee of any attempt by his creditors or other persons to evade the provisions of this act that come to his knowledge", § 7 (6) and "in case of any person having to his knowledge proved a false claim against his estate, disclose that fact immediately to his trustee", § 7 (7). These duties were performed in the city of Seattle, Mr. MacDonald's place of residence and were exactly what, under the sections above quoted, he was required to perform.

There was some claim made before the referee that these provisions apply only to individual bankrupts and not to the officers of a bankrupt corporation, but under the definitions which we have heretofore quoted, contained in § 1 of the Bankruptcy Act, the term "bankrupt" includes the officers of a corporate bankrupt. Furthermore, if there is no duty upon the officers of a bankrupt corporation to perform the duties required under the bankruptcy act by an individual bankrupt, the hands of the bankruptcy courts

would be absolutely tied in the case of a corporate bankrupt. The duties which Mr. MacDonald performed in assisting in the contesting of the claims of the Australian Government were only those duties, performed at his place of residence, he was required to perform under the Bankruptcy Act. He was not entitled to be reimbursed for his expenses upon his trip to Washington because no proper statement of such expenses was ever furnished and the statement which was furnished was palpably false upon its face.

One exception taken by this petitioner was that no segregation of the allowance was made for these three different items: the expenses, the services in presenting the claim against the Shipping Board, and the services in contesting the claim of this petitioner. The order of the referee, however, which was approved by the District Court, lumped the three matters together and granted Mr. MacDonald $20,000 in full for the entire claim. Even if he was entitled to compensation for his services in Washington, it was absolutely impossible to determine how much was allowed for this and how much for the other two items. Therefore, while it may be the law that the amount which a referee may allow for compensation is within the sound judicial discretion of the referee, nevertheless, where he makes an allowance for items which are clearly contrary to the Bankruptcy Act and these items are included in a blanket allowance so that it is impossible to separate the good from the bad, the situation is identical with that where in a jury trial, the court sub-

mits to the jury different elements of damage, one of which is correct and two of which are incorrect, and the jury brings in one general verdict It is impossible to determine what was the allowance upon each item and therefore, the entire allowance must be set aside.

One of the exceptions which the petitioner took to the action of the referee in this case (which by the way was one which the referee absolutely ignored in his certificate), was that there was no sworn statement regarding this claim. The Bankruptcy Act expressly provides for the allowance of fees to attorneys for trustees and petitioning creditors and to trustees and referees, but there is no express provision in the Bankruptcy Act providing for fees for services to be allowed to the bankrupt for services rendered to the estate. The only guise under which such an allowance can possibly be made is that it is an expense of the trustee necessarily incurred in the administering of the estate, but § 62 provides that the expenses of administering the estate incurred by officers "shall, except where other provisions are made for the payment, be reported in detail under oath and examined or disapproved by the court". No slightest attention was paid by the referee to this section, and the exception of this petitioner upon this ground did not even so much as receive a mention in the referee's certificate.

A careful search of the reports fails to indicate a single instance where an officer of the bankrupt has ever been allowed any compensation for services rendered to the trustee, except one case which was cited by

the respondent in the lower court, being *In re Barrow*, 98 Fed. 582, where the bankrupt was allowed compensation for work and care bestowed upon crops after the date of his adjudication of bankruptcy. There could be no question but that this was a service which was necessary for the physical protection of the estate and the bankrupt would be as much entitled to pay therefor as any other person. The only cases in the district courts where claims have ever been made by bankrupts for compensation in connection with testifying and the like is the case of *In Re Barnes,* Fed. Cas. 1013, decided in the District Court for the Eastern District of Pennsylvania, Oct. 7, 1874, which opinion reads as follows:

> "The bankrupts having made a claim for services rendered the estate, the same was disallowed by the register, whereupon they excepted to the register's decision.
>
> The Court said: 'As to questions of special allowance to the bankrupts, or any of them, the court perceives no sufficient reason for directing such an allowance. This does not, however, necessarily preclude the allowance of something under this head by the creditors, of grace, if the bankrupts have rendered extraordinary services, beyond those required in order to make the property, rights, credits, and effects available."

In two cases, *In re McNair,* Fed. Cas. 8907, and *In re O'Kell,* Fed. Cas. 10,474, it was held that a bankrupt was not entitled to witness fees for attendance at his examination, and in two cases, *In re Lane Lumber*

*Co.*, 206 Fed. 780, 783, and *In re Medina Quarry Co.*, 182 Fed. 508, it was specifically held that the attorney of the bankrupt was not entitled to an allowance for assistance rendered to the trustee in defeating claims where the trustee was also resisting such claims.

This is the entire case law upon this question although the present Bankruptcy Act has been in force for over twenty-five years, and during that time many bankrupts and officers of bankrupt corporations have given much of their time and energy in unraveling involved estates, but there is not a single reported case where compensation was even so much as claimed therefor except in these which we have just cited.

We respectfully submit that this allowance to Mr. MacDonald was clearly erroneous and should be set aside.

Respectfully submitted,

CORWIN S. SHANK,

*Attorney for Petitioner.*